



## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-75065; File No. SR-ICEEU-2015-005]

May 28, 2015

Self-Regulatory Organizations; ICE Clear Europe Limited; Order Approving Proposed Rule Change Relating to CDS Procedures for CDX North America Index CDS Contracts

### I. Introduction

On February 12, 2015, ICE Clear Europe Limited (“ICE Clear Europe”) filed with the Securities and Exchange Commission (“Commission”) a proposed rule change pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to revise ICE Clear Europe’s CDS Procedures, CDS Risk Model Description and CDS End-of-Day Price Discovery Policy to provide the basis for ICE Clear Europe to clear CDX North America Index CDS Contracts (“CDX.NA Contracts”). The proposed rule change also includes revisions to the CDS Procedures that relate to iTraxx Contracts and single name CDS Contracts. The proposed rule change was published for comment in the Federal Register on March 2, 2015.<sup>3</sup> On April 16, 2015, the Commission extended the time period in which to either approve, disapprove, or institute proceedings to determine whether to disapprove the proposed rule change to May 31, 2015.<sup>4</sup> The Commission did not receive comment letters regarding

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Securities Exchange Act Release No. 34-74362 (Feb. 24, 2015), 80 FR 11246 (Mar. 2, 2015) (File No. SR-ICEEU-2015-005).

<sup>4</sup> Securities Exchange Act Release No. 34-74741 (Apr. 16, 2015), 80 FR 22593 (Apr. 22, 2015) (File No. SR-ICEEU-2015-005).

the proposed change. For the reasons discussed below, the Commission is granting approval of the proposed rule change.

## II. Description of the Proposed Rule Change

ICE Clear Europe has submitted proposed amendments to its CDS Procedures to (i) revise the CDS Procedures to add a new section containing contract terms applicable to the CDX.NA Contracts that ICE Clear Europe proposes to accept for clearing; (ii) make conforming changes throughout the CDS Procedures to reference the CDX.NA Contracts; and (iii) make certain other clarifications, corrections and updates to the CDS Procedures (including for iTraxx Contracts and Single Name Contracts), as discussed in more detail herein. ICE Clear Europe has also proposed to make certain modifications to its CDS Risk Model Description and CDS End-of-Day Price Discovery Policy (the “CDS Pricing Policy”) to accommodate clearing of CDX.NA Contracts, as described herein.

ICE Clear Europe has proposed to amend Paragraphs 1, 4, 6, 9, 10 and 11 of the CDS Procedures, described below. All capitalized terms not defined herein are defined in the ICE Clear Europe Clearing Rules (the “Rules”).

In paragraph 1 of the CDS Procedures, references will be added to the defined terms “iTraxx Contract” and “CDX.NA Contract,” as such terms are set out in revised paragraphs 9 and 10 of the CDS Procedures, respectively. The definition of “Original Annex Date” will be modified to apply to CDX.NA Contracts in substantially the same manner it applies to iTraxx Contracts. In addition, the definition of “Protocol Excluded Reference Entity” in former paragraph 10.3 will be changed to “Protocol Excluded Corporate Reference Entity” and moved to paragraph 1, to reflect that such term is only used in the context of corporate reference entities. Accordingly, the definition will be

revised to mean an Eligible Single Name Reference Entity that is a Standard European Corporate (as specified in the List of Eligible Single Name Reference Entities) and is an Excluded Reference Entity (as defined in the 2014 CDD Protocol). (Conforming changes will be made to references to that definition throughout the CDS Procedures.) In addition, a correction will be made to the cross-reference in definition of “New Trade” to properly refer to the definition set out in the applicable Contract Terms for the relevant contract.

In addition, amendments will be made to use the defined terms “Component Transaction” and “Clearing” throughout the Procedures in lieu of the undefined terms. Finally, various conforming references to the new or revised defined terms will be made throughout the CDS Procedures, various provisions of the CDS Procedures will be renumbered, and certain cross-references to prior paragraph 1.71 will be corrected.

Various clarifications will be made in Paragraph 9 of the CDS Procedures, which sets out the contract terms for iTraxx Contracts. Specifically, paragraph 9.1 will be modified to clarify that it specifies the additional Contract Terms applicable to all iTraxx Contracts cleared by the Clearing House. Paragraph 9.2(c)(i), which applies to iTraxx Contracts which are governed by the Standard iTraxx 2014 CDS Supplement, will be modified to make certain additional clarifications relating to initial payments and spun-out trades. Paragraph 9.2(c)(i)(B) will be added to reflect current clearing house (and market) practice that initial payments under cleared iTraxx Contracts (other than those for which a bilateral transaction is already recorded in Deriv/SERV) are made on the business day following the trade date (or, if later, the business day following the date of acceptance for clearing). New paragraph 9.2(c)(i)(D), which will address the reference

obligation for a spun-out trade following a restructuring credit event, is substantially the same as the corresponding language in paragraph 9.3(c)(i)(D) for contracts subject to the Standard iTraxx Legacy CDS Supplement and was inadvertently omitted from prior amendments. A cross-reference in paragraph 9.2(c)(i)(E) will be updated. New paragraph 9.2(c)(i)(F) will provide that paragraph 5.7 of the Standard iTraxx 2014 CDS Supplement, which contains restrictions on delivery of Credit Event Notices and Successor Notices, does not apply to iTraxx Contracts (as the appropriate restrictions in the context of a cleared transaction are already addressed in the Rules and CDS Procedures, including Rule 1505).

As set forth in paragraph 9.2(c)(ii), changes will also be made to the terms of the iTraxx 2014 Confirmation with respect to iTraxx Contracts that are governed by the Standard iTraxx 2014 CDS Supplement. These amendments will include a clarification that references to the 2014 Credit Derivatives Definitions in the standard supplement and confirmation will be interpreted for cleared contracts as though they have the meaning ascribed to that term in the Rules and Procedures. In addition, a provision that there are no “Omitted Reference Entities” for purposes of the standard confirmation will be removed as that term is not used in the standard supplement and confirmation and is therefore unnecessary.

Similar clarifications will be made in paragraph 9.3, which relates to iTraxx Contracts which are governed by the Standard iTraxx Legacy CDS Supplement. Specifically, new paragraph 9.3(c)(i)(B) will contain the same clarification discussed above with respect to the initial payment date for a contract. Paragraph 9.3(c)(i)(D) will contain a correction that the treatment therein of reference obligations for spun-out trades

applies for reference entities subject to both Sections A and B of the Standard iTraxx Legacy CDS Supplement (that is, both protocol- excluded and non-excluded entities). Subparagraph (F) will provide that restrictions under the standard supplement as to delivery of Credit Event Notices and Succession Event Notices do not apply, as the issue is otherwise addressed under the Rules and CDS Procedures, as discussed above. In paragraph 9.3(c)(ii)(E), a reference to there being no “Omitted Reference Entities” will also be removed for the reasons noted above.

New paragraph 10 of the CDS Procedures will be added to set out the contract terms for CDX.NA Contracts. Paragraph 10.1 will provide that different sub-provisions of paragraph 10 will apply to CDX.NA Contracts depending on whether the Original Annex Date for the relevant index series falls before or after the Protocol Effective Date.

New paragraph 10.2 will apply to CDX.NA Contracts with an Original Annex Date on or after the Protocol Effective Date (i.e., for transactions in the September 2014 or later versions of the index). New definitions will be added to subparagraph (a), including definitions for “CDX.NA Contract”, “CDX.NA Publisher”, “CDX.NA Terms Supplement”, “Eligible CDX.NA Index”, “List of Eligible CDX.NA Indices”, and “Relevant CDX.NA Terms Supplement”, which largely track the analogous definitions in paragraph 9 with respect to iTraxx Europe Contracts. Paragraph 10.2(b) will incorporate defined terms from the Relevant CDX.NA Terms Supplement and also will contain an inconsistency provision which provides that paragraph 10.2 governs over the CDX.NA 2014 CDS Supplement and CDX.NA 2014 Confirmation. Paragraph 10.2(c) will contain certain amendments to the Standard CDX.NA 2014 CDS Supplement and CDX.NA 2014 Confirmation, which are generally consistent with the amendments to the iTraxx 2014

Terms Supplement and iTraxx 2014 Confirmation in paragraph 9.2(c) and are generally designed to accommodate the requirements of clearing and make the standard contract terms consistent with the Rules and Procedures. In addition, paragraph 10.2(c)(i)(E) will address the application of the defined term “Index Party” in the standard supplement in the context of a cleared transaction, and paragraphs 10.2(c)(ii)(E)-(F) will be added to refer to certain transaction terms specified in the List of Eligible CDX.NA Indices for the relevant index and tenor. Paragraph 10.2(c)(i)(G) will clarify that as with iTraxx Contracts, de minimis cash settlement under the standard supplement does not apply. Paragraph 10.2(c) will also indicate the transaction terms that must be specified in the submission of a trade for clearing.

New paragraph 10.3 will apply to CDX.NA Contracts with an Original Annex Date before the Protocol Effective Date (i.e., for transactions in older versions of the index). Paragraph 10.3 will contain definitions and provisions generally similar to those in paragraph 10.2, and make comparable amendments to the Standard CDX.NA Legacy CDS Supplement and the CDX.NA Legacy Confirmation.

New paragraph 10.4 will contain procedures for updating the CDX.NA index version following a Credit Event or Succession Event. These provisions will be generally consistent with the comparable provisions for iTraxx contracts in paragraph 9.8. New paragraph 10.4(b) will add a similar procedure for implementing a new version of the CDX.NA standard terms supplement, if and when published, where contracts referencing the old and new versions of the supplement are determined by the Clearing House to be fungible.

Existing paragraph 10, which contains contract terms for Single Name Contracts, will be renumbered as paragraph 11 and cross references will be updated accordingly. In addition, various clarifying amendments will be made to this paragraph. The definitions of “STEC Contract” and “Non-STEC Single Name Contract” will be amended to clarify that the relevant Reference Entity type will be specified in the List of Eligible Single Name Reference Entities. The definition of “Single Name Contract Reference Obligations” will be amended to clarify that the applicable reference obligation will be specified in the List of Eligible Single Name Reference Entities and may differ between 2003-type CDS Contracts and 2014-type CDS Contracts. For 2014-type CDS Contracts, the reference obligation may be designated as the Senior Level Standard Reference Obligation that is specified from time to time on the SRO List published under the 2014 ISDA Definitions.

Paragraph 11.6(a)(i)(C) will be amended by adding a subsection (2) that will make a clarification as to the initial payment date for Single Name Contracts that corresponds to the change in payment date discussed above for iTraxx Contracts. A change will be made in paragraph 11.6(a)(ii) to conform to the changes made to the definition of Single Name Contract Reference Obligation discussed above.

In general, under ICE Clear Europe’s proposal, the existing risk methodology that applies to index CDS will also apply to the CDX.NA Contracts. However, ICE Clear Europe proposes to make certain amendments to its CDS Risk Model Description and CDS Pricing Policy to address CDX.NA Contracts.

In the CDS Risk Model Description, the index decomposition offset methodology, which is used to determine portfolio margin benefits from correlated long and short

positions, is proposed to be modified to address multi-region risk factors. Under the revised methodology, portfolio margin benefits are provided first for risk factors within the same region. After the same-region risk analysis is completed, any cross-region benefits for index risk factors are determined. Cross-region benefits apply only to index risk factors. The revised description thus addresses scenarios in which margin offsets may be provided between appropriately correlated positions in iTraxx Contracts and positions in CDX.NA Contracts. The revisions also provide that where risk factor profits and losses are calculated in different currencies, they will be converted into the same base currency (Euro) for purposes of calculation of portfolio margin benefits.

ICE Clear Europe also proposes to amend its CDS Pricing Policy to cover the CDX.NA Contracts. The amendments include submission requirements with respect to CDX.NA Contracts and changes to reflect that certain determinations with respect to firm trades for CDX.NA Contracts are made as of the North American end-of-day.

### III. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act<sup>5</sup> directs the Commission to approve a proposed rule change of a self-regulatory organization if the Commission finds that such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such self-regulatory organization. Section 17A(b)(3)(F) of the Act<sup>6</sup> requires, among other things, that the rules of a clearing agency are designed to promote the prompt and accurate clearance and settlement of securities transactions and,

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<sup>5</sup> 15 U.S.C. 78s(b)(2)(C).

<sup>6</sup> 15 U.S.C. 78q-1(b)(3)(F).



to the extent applicable, derivative agreements, contracts, and transactions and, in general, to protect investors and the public interest.

The Commission finds that the proposed rule change is consistent with Section 17A of the Act<sup>7</sup> and the rules thereunder applicable to ICE Clear Europe. The proposed rule change will provide for clearing of the CDX.NA Contracts, which are similar to the index CDS Contracts currently cleared by ICE Clear Europe, in accordance with existing rules and procedures. Specifically, the Commission believes that ICE Clear Europe's proposal to clear the CDX.NA Contracts pursuant to its risk management framework, operational procedures, end-of-day pricing policies, settlement procedures and default management policies (as modified by the proposed rule change) is designed to promote the prompt and accurate clearance and settlement of securities transactions, derivative agreements, contracts, and transactions, and in general, to protect investors and the public interest, consistent with Section 17A(b)(3)(F) of the Act.<sup>8</sup> The Commission further believes that the clearing of CDX.NA Contracts in accordance with ICE Clear Europe's existing CDS risk policies (including margin and guaranty fund), as modified by the proposed rule change, is reasonably designed to meet the requirements of Rules 17Ad-22(b)(1) - (3)<sup>9</sup> related to the measurement and management of credit exposures, margin requirements, and the maintenance of sufficient financial resources required for a registered clearing agency acting as a central counterparty for security-based swaps.

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<sup>7</sup> 15 U.S.C. 78q-1.

<sup>8</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>9</sup> 17 CFR 240.17Ad-22(b)(1) - (3).

Additionally, the Commission believes that the proposed rule change, as it relates to various clarifying and conforming changes with respect to iTraxx Contracts and single name CDS Contracts, is designed to promote the prompt and accurate clearance and settlement of securities transactions and in general, to protect investors and the public interest, consistent with Section 17A(b)(3)(F) of the Act.<sup>10</sup>

The Commission therefore finds that the proposed rule change is designed to promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions and, in general, to protect investors and the public interest in accordance with Section 17A(b)(3)(F) of the Act.<sup>11</sup>

#### IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act<sup>12</sup> and the rules and regulations thereunder.

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<sup>10</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>11</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>12</sup> 15 U.S.C. 78q-1.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>13</sup> that the proposed rule change (File No. SR-ICEEU-2015-005) be, and hereby is, approved.<sup>14</sup>

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>15</sup>

Brent J. Fields,  
Secretary.

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<sup>13</sup> 15 U.S.C. 78s(b)(2).

<sup>14</sup> In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

<sup>15</sup> 17 CFR 200.30-3(a)(12).